Eliminate Environmental Roadblocks Through Insurance

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Too often, concerns over environmental contamination impede negotiations in business transactions — especially those involving commercial property. These environmental risks can take many forms: known or potentially unknown on-site contamination, liability for off-site contamination (e.g., through waste disposal or transport activities), the acquisition of environmental liabilities through assumed contracts and so on. At the negotiating table, these risks can become a game of hot potato, with neither party willing to assume them post-closing. Absent a solution, they can even be deal-killers. Savvy parties, however, recognize another option: insurance.

Through insurance, parties can liquidate their risk in the form of an insurance premium, passing the real risk of loss onto an insurer. Unfortunately, even those savvy enough to consider insurance often fail in one key regard: they do not treat the procurement of insurance as a specialized business transaction. Instead, all too often, parties task their insurance brokers, as skilled as they are, with the critical (and more suitably, legal) task of assessing whether proposed policy language encompasses the environmental risks identified. In doing so, they perform the insurance analog of forgoing legal counsel in favor of sole reliance on a real estate agent, when the two roles should be complimentary. The annals of insurance litigation tell many a tale of parties that shortchanged the insurance procurement process. Those that chose to do so missed opportunities to mitigate their risk. Worse still, they often ended up paying for coverage that afforded no real protection.

For these reasons, many parties dealing with complex environmental issues today turn to environmental coverage counsel to advise on mitigating environmental risk in business transactions. Not only can environmental coverage counsel advise on the procurement of the correct insurance for the risks identified, but they can also evaluate alternative insurance solutions in transactions (e.g., the availability of existing coverage) to address the risks identified.

I. Environmental Coverage Can Be Challenging To Procure Correctly

Critical to assessing the need for, and utility of, environmental insurance is having a nuanced understanding of the environmental risks to which one is subject. This may include risks associated with past on-site operations, off-site activities related to on-site operations (such as waste disposal for CERCLA liability), or third-party activities that may create on-site conditions. Protecting against these risks can certainly come in the form of a new insurance policy, but protections may already be in place in the form of existing coverage that a buyer can obtain from a seller through its transaction. Whether buying new coverage or acquiring existing coverage, however, pitfalls abound.

A. Looking to New Polices

There are several insurance products that can help address environmental risks. Examples include:

- General liability and commercial property policies, which can be modified to provide limited degrees of environmental coverage

- Site-oriented pollution legal liability policies that, when properly tailored, can cover all manner of environmental losses and liabilities
- Contractor pollution policies that are designed to cover specific operations

Conceptually, there is a product for nearly every risk. There are even products designed to limit excess cleanup costs in connection with a known contamination (i.e., remediation cost cap insurance), and some insurers are even willing to issue policies that insure against liabilities associated with known contamination.

As with everything, the devil is in the details. The insurance market, like the stock market, runs in cycles and insured parties face a hardening insurance market. Many insurers are now refusing to issue certain policy types, such as remediation cost cap insurance. Others are heavily restricting their standard terms through endorsements to afford only a subset of the coverage they once did—e.g., not covering first-party cleanup or only covering cleanup when ordered by a governmental agency. The effect of these restrictions is heavily dependent on the policy language employed. As such, one of the first steps to finding the right coverage is not only knowing the available players in the market (for which a broker's advice is invaluable) but also understanding the ramifications of the specifics of the policy language. For example, there can be considerable differences in how certain states interpret the concept of "cleanup costs." This can lead to radically different coverage outcomes based on what may ostensibly seem to be similar policy language. Fortunately, insured parties savvy enough to identify and address those issues can often re-contour their coverage to secure the protection needed. Explained below, these issues are almost always best addressed with the aid of coverage legal counsel.

Another recurrent issue is procuring coverage for known risks and particularly known contamination. For example, many policy forms contain exclusions for known conditions, which need to be addressed through endorsements to afford the required coverage. Even more insidiously, when a policy does not contain such an exclusion, carriers have been known to argue that state common law "known loss" and "known risk" doctrines apply to prohibit or limit coverage. Fortunately, despite these issues, they can be avoided though a careful choice of law analysis and the deployment of policy terms that avoid these results under applicable law.

B. What Coverages Already Exist?

For parties looking to tap into existing coverage to allay environmental concerns, the inquiry is generally twofold:

1. Whether existing policies afford coverage for the environmental concerns
2. Whether the buyer can effectively tap them for coverage

When assessing policies for potential coverage for environmental issues, one should start by looking at general liability policies, pollution legal liability policies and contractor pollution liability policies. For first party losses, one might also consider commercial property policies. These policies serve as the frontline defense for pollution risks — although there may be other policies providing limited coverage worth assessing, along with any policies of third parties that may insure the seller as an additional insured. With respect to general liability policies in particular, the principal question is whether the policies contain a pollution exclusion (generally, older polices contain no or weaker variants) and whether applicable law construes those exclusions to bar the environmental concerns in question. While that inquiry can be rather nuanced, in simplest terms, certain states have construed pollution exclusions more narrowly to preserve coverage in many contexts, warranting a review of applicable law.

With respect to whether the buyer can effectively tap into the coverage it identifies, there are several issues that need to be run down. First, a company may have policies going back decades. This opens the door to a series of issues associated with historical coverage: finding lost policies, determining which polices have remaining limits, assessing insurer solvency and so on. These hurdles are often well worth the energy to surmount. Older policies — particularly general liability policies — are more forgiving when it comes to pollution coverage. Polices from the 1960s may have no pollution exclusion, while policies from then-on have increasingly stronger pollution exclusion language. In short, it may be that a seller's policy from the 1970s can absorb the risk identified, at least when the conduct in question occurred in part at that time, whereas a modern general liability policy could not. Ultimately, such a review turns not only on the form of the policy, but in how such policies have been construed under applicable law. As such, a historical policy assessment by coverage counsel is generally required to reap the benefit of historic coverage.

Another concern can be anti-assignment provisions in the insurance policies. State law varies considerably in terms of the effect of such language. Some states recognize an exception to anti-assignment provisions when dealing with a loss or harm that has already occurred at the time of the transaction. The gist being that once the loss has occurred, the right to receive policy benefits for that loss can be assigned without assigning the entire policy (i.e., swapping who the policy insures). Again, the extent to which an anti-assignment provision may apply is a question of local law.

II. Environmental Coverage Counsel Is Often Key to Effectively Eliminating Risk

Historically, coverage lawyers have been litigators, either representing policyholders (as Haynes Boone does) or insurance companies in disputes over coverage for losses and liabilities that have arisen. As insurance has increasingly been deployed to address risks in transactions, a new subset of coverage lawyers has arisen to focus on helping clients reduce risk through insurance in business transactions.

In the realm of environmental risk, it was once common for companies simply to task their environmental counsel to assess the risks and their broker to find the right insurance for those risks. In their discrete wheelhouses of assessing environmental risks and procuring insurance for a competitive price, each excelled. That relationship had several weaknesses, often leading to a failure to fully align those risks with coverage. Through no fault of their own, environmental counsel lacked the experience to ascertain whether the environmental risks they identified were sufficiently captured by terms quoted by insurers. Similarly, environmental counsel would prove ill-equipped to analyze available historical coverage. Conversely, brokers were ill-equipped to grapple with many of the legal nuances of the risks identified (e.g., the complexities of CERCLA liability), which were often critical to procuring the correct coverage. They too were ill-equipped to perform the legal analyses needed to ensure policy terms would be applied as intended under applicable law, and to assess historical coverage. Finally, unlike lawyers, brokers are subject to the economic driver that they are paid to close on insurance policies, not spot issues. In the end, each of these weaknesses introduced the potential for missed opportunity — or worse, the potential to pay for insurance that ultimately provided no protection.

The need for advice that bridged the gap between the expertise of environmental counsel and brokers gave rise to a subniche of coverage lawyer: coverage lawyers focusing on environmental risks in business transactions. Their practice exists to eliminate the communication gaps that too often arise between environmental counsel and brokers. These attorneys work with environmental lawyers to understand the legal contours of the risks identified and work with brokers to ensure the policies being procured have been property vetted (and if necessary, tailored) to maximize coverage for those exact risks under applicable law. Further, coverage counsel can perform the

analysis required to assess existing coverage as a potential solution. These many benefits, particularly in large transactions involving particularly complex environmental risks, have made environmental coverage lawyers an integral part of many modern deal teams.

Conclusion

Parties faced with environmental risks in their deals should almost always consider insurance as a potential solution. If those risks can be successfully shifted to an insurer, it removes one more issue from the negotiating table. Environmental risks can be notoriously tricky to insure. Procuring the right coverage requires more than a sophisticated broker to navigate the insurance market, as it requires a legal analysis of the environmental risk in combination with the proposed coverage to ensure the program put in place is not unknowingly undermined. That is why clients facing such risks are often well-advised to seek the advice of coverage counsel when evaluating coverage.[1]

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